CIPFA The Chartered Institute of Public Finance & Accountancy

report

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Committee	CIPFA/LASAAC
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Subject	Streamlining the Presentation of Local Authority Financial Statements

To consider the proposals in the Invitation to Comment on the Streamlining of the Presentation of the Financial Statements and the Exposure Draft of the proposed changes to the Code.

1 Introduction

1.1 CIPFA/LASAAC considered the options presented by the Streamlining Working Group at its March 2015 meeting. The Board was content that the Review should pursue option 4 and option 2 which were to introduce the new Funding Statement and IFRS based Comprehensive Income and Expenditure Statement and the Movement in Reserves Statement with all three statements reflecting the circumstances of the individual local authority. CIPFA/LASAAC also agreed that the latter two IFRS based statements should be reduced to their absolute minimum.

1.2 The Invitation to Comment (ITC) on the Streamlining Review has been structured in such a way that it allows levels of accessibility to the document. The ITC includes a Foreword to describe in plain language the reasons for the review and provide an "at a glance" summary of the changes in one page. The ITC then includes an executive summary of the changes with a full list of the questions. The last section of the ITC includes a detailed and technical analysis so that the changes can be assessed against the requirements of IFRS and to ensure that the proposals also reflect local government circumstances.

1.3 The Streamlining Review Working Group (Working Group) was able to consider an early draft of the Invitation to Comment, the Example Appendices and the Exposure Draft of Section 3.4 of the Code. The comments of individual members have been included, where possible; the comments were all generally supportive of the approach.

1.4 As the proposals have an impact on the role of the Service Reporting Code of Practice and thus potentially on the role of government statistical returns the Secretariat has met with each of the devolved administrations to ensure that any relevant and consequential issues are raised.

1.5 One of the most difficult issues for local authorities is that they have a wide range of possible users of the financial statements, this range being wider and much more diverse than the private sector and even possibly other parts of the public sector. The ITC therefore outlines the debate of the Working Group on the users of local authority financial statements with the Working Group aim of making the financial statements as accessible as possible to all but with the priority being given to council tax and non-domestic rate payers.

2 Funding Statement

2.1 Following the debate at the last meeting of CIPFA/LASAAC the Funding Statement has been prioritised in the proposals as the new statement performs a link between the two frameworks ie the funding framework and the accounting framework. Following comments at the last meeting, the Statement now starts from the funding position ie the General Fund (net expenditure chargeable to taxation and rents) and reconciles back to the Comprehensive Income and Expenditure Statement net expenditure column. The Funding Statement is also presented based on the segments ie the department structure that an individual local authority operates.

2.2 As the Housing Revenue Account (HRA) is a statutorily ringfenced element of the General Fund the Funding Statement includes a consolidated HRA. The Secretariat considers appropriate analysis is provided in the separate HRA Income and Expenditure Statement and Movement on the Housing Revenue Account Statement. One of the main reasons for this is the issue of readability and understandability of the Statement. One of the Working Group Members, however, did suggest that a separate Funding Statement should be provided for the HRA. **CIPFA/LASAAC's views are sought on this issue**.

2.3 It is very difficult to present comparators and more difficult for users to understand information when more than three columns are presented. The Working Group wanted to ensure that the Funding Statement could be understood by the widest range of users and therefore this statement needed to be as easily accessible as possible.

2.4 In accordance with CIPFA/LASAAC's request the Funding Statement also includes a reconciliation to General Fund Balances at the foot of the Statement. This reconciliation is split between the General Fund and the HRA to ensure that there is clarity for the users of the financial statements of the Council's usable resources.

2.5 At the last meeting of CIPFA/LASAAC there was substantial debate on whether the Funding Statement should include information on the budget. Supported by the overall comments of the Working Group members the Secretariat has included the Funding Statement without budgetary information. However, if budgetary information is included in the main financial statements this would mean that this information would have to be considered as an element of the "true and fair" opinion. This might raise issues of auditability as budgetary information by its nature less easy to assess against audit assertions and is often appropriately subject to change.

2.6 The ITC does raise this as an issue (and includes an appropriate question). It also considers that the Narrative Report should include appropriate budgetary comparison to the outturns in the Funding Statement.

2.7 CIPFA/LASAAC will have noted that the ED has included the Funding Statement as the first statement and has included it in the IAS 1 based listing of a complete set of financial statements. The ED also includes he specifications for a Funding Statement identifying what would need to be reported in the three columns of the Funding Statement. There is no model in IFRS for this Statement and the Secretariat would seek the Board's views on whether or not the reporting requirements in draft paragraph 3.4.2.39 capture the reporting requirements of the Funding Statement.

2.8 The ITC also seeks interested parties' views on whether comparative information should be provided in the Funding Statement. As a non-IFRS based Statement CIPFA/LASAAC could decide not to include comparative information. Section 5 of this report sets out proposals for the Funding Statement to provide substantial elements of the segmental reporting requirements under IFRS 8 *Operating Segments*. If these proposals are accepted then the Funding Statement as a part of meeting the requirements of IFRS would need to include comparative information.

2.9 CIPFA/LASAAC will note that the Funding Statement relies on net reporting requirements for both the General Fund and the CIES. Most financial reporting requirements start from a gross base. The gross information for the CIES column is provided in the CIES. The Secretariat considers that clear and understandable comparison of the two frameworks can only be on a net basis but would welcome CIPFA/LASAAC's views on this issue.

CIPFA/LASAAC is invited to consider the approach outlined in the ITC and Exposure Draft for the Funding Statement.

3 Comprehensive Income and Expenditure Statement

3.1 The Comprehensive Income and Expenditure Statement is also included in the proposals following the same format that was presented to CIPFA/LASAAC previously and is based on the organisational structure under which an authority operates. To ease the reporting burden and continue the theme of allowing authorities to report under their own structure the proposals require that the segmental analysis is provided on a direct "accrued" cost basis and not the definition of total cost in SeRCOP.

3.2 There are a small number of areas where this may not be appropriate ie the reporting of discontinued services where it is possible that overheads may need to be reported and the reporting of any trading accounts which would also need to be on a total cost basis.

3.3 Following discussions at CIPFA/LASAAC's last meeting the Secretariat has also moved the Code's provisions on the CIES before that of the Movement in Reserves Statement to reflect the trail from the Funding Statement. However, in accordance with previous editions of the Code the order of statements remains a recommendation allowing local authorities the opportunity to structure the statements in accordance with the needs of their users.

CIPFA/LASAAC is invited to consider the approach outlined in the ITC and Exposure Draft for the Comprehensive Income and Expenditure Statement.

4 Movement in Reserves Statement

4.1 The proposals for change in the Movement in Reserves Statement (MiRS) include (as discussed at the last meeting) reducing the MiRS to the absolute minimum that meets the objectives for the Statement. The proposals therefore exclude information about transfers between earmarked reserves. In addition the movements from the CIES are consolidated into one line ie the Total Comprehensive Income and Expenditure (as the columnar analysis of the usable and unusable reserves automatically separates the movements between the Surplus and Deficit on the Provision of Services and Other Comprehensive Income and Expenditure).

4.2 Where authorities consider that they need to report their earmarked reserves on the face of the MiRS, draft paragraph 3.4.2.56 permits them to do this.

4.3 The ITC discusses which reserves to include on the face of the MiRS to comply with IAS 1 ie the reserves would need to show the movements in the components of equity. The ITC adds that this is necessary to demonstrate accountability for resources utilised against these statutorily defined reserves. In addition, if these reserves were not included on the face of the MiRS, they would need to be included in the notes to that statement. Effective presentation of these reserves in one statement therefore will assist in the streamlining of local authority statements.

CIPFA/LASAAC is invited to consider the approach outlined in the ITC and Exposure Draft for the Movement in Reserves Statement.

Notes to the Movement in Reserves Statement

4.4 The feedback on the consultations and the review of the financial statements demonstrated that one of the most difficult notes to present is the requirement in paragraph 3.4.2.40 (of the 2015/16 Code) to provide an analysis of line item g) – adjustments between the accounting and funding basis. CIPFA/LASAAC made amendments to the 2015/16 Code to encourage simplification of the presentation of the requirements. The proposed paragraph 3.4.2.56 now adds for clarity that all of the items do not have to be individually identified in the analysis.

4.5 The Secretariat considers that it can propose this as a number of the items of this disclosure should be available in the other notes of the authority (eg property, plant and equipment notes should include depreciation and impairment and capital financing charges such as the Minimum Revenue Provision). Some of this information should also be available in explanation of the adjustments between the General Fund and the CIES in the Note to the Funding Statement.

4.6 The amendments also include an explicit requirement for an analysis of material earmarked reserves as they are no longer included on the face of the MiRS.

4.7 Appendix 6 provides a demonstration of how the note to the MiRS could be presented. This is still quite a complex disclosure but is substantially reduced from the majority of examples seen by the Secretariat.

CIPFA/LASAAC is invited to consider the approach outlined in the ITC and Exposure Draft for the Notes to the MiRS.

5 Segmental Analysis

5.1 CIPFA/LASAAC members will be aware that other than the notes to the MiRS the segmental reporting requirements represent the area subject to most comment when opportunity has been given in previous consultations. This might in part be because local authorities had to provide two segmental analyses, one under SeRCOP analysis and one meeting the requirements of IFRS 8 to analyse information on the basis of how authorities "allocate resources to and assess the performance of the operating segments of the entity".

5.2 The proposals for the Funding Statement and the CIES therefore include substantial segmental information both on the basis of how local authorities present information to the Chief Operating Decision Maker (CODM) (note that this is interpreted in the Code as a single CODM does not exist in local authorities) and which reconciles to the Surplus or Deficit on the Provision of Services. The Working Group does not consider that the items of income and expense, for example, depreciation in paragraph 28 of IFRS 8 *Operating Segments,* are regularly reported to the CODM and therefore the specified costs and resultant reports are unlikely to apply, though the ITC explores this issue with authorities.

5.3 Paragraphs 28 a) and b) of IFRS 8 require that the total of the reportable segments' revenues reconciles to the entity's revenue and the total of the reportable segments' measures of profit or loss to the entity's profit or loss before tax expense (tax income) and discontinued operations. The Working Group considers that the format of the Funding Statement provides a reconciliation in the CIES as its segmental information matches to the Surplus or Deficit on the Provision of Services (the equivalent of profit or loss).

5.4 Paragraph 28 of IFRS 8 also requires that "all material reconciling items shall be described". Therefore each of the columnar adjustments "*Adjustments between Funding and Accounting (IFRS)* basis that reconcile the General Fund and HRA balances in the Funding Statement to the CIES would need to be analysed for material items. An example format of the adjustments Note is provided in Appendix 3. Note this is positioned at Appendix 3 to facilitate an easy read through for interested parties.

5.5 The current arrangements for segmental information in the 2015/16 Code state that the analysis of total income and expenditure also satisfies the requirement in IAS 1 to present information regarding the nature of expenses. This will not be provided in the Funding Statement. Therefore a new paragraph 3.4.2.45 has been proposed to meet these requirements of IAS 1.

CIPFA/LASAAC is invited to consider the approach to the segmental analysis in the ITC including the Appendix and the Exposure Draft of the Code.

6 The Role of the Service Reporting Code of Practice and the Impact of the Proposals on Statistical Returns

6.1 The ITC highlights the issue of the impact of the removal of the SeRCOP reporting requirements from the financial statements. The Secretariat has arranged discussions with the government departments from the devolved administrations that request information on the basis of the SeRCOP Service Expenditure and a form of total cost to discuss the impact of this change. The ITC emphasises that the removal of the requirements from the financial statements does not change the status of SeRCOP as a proper practice (in the jurisdictions where this applies). It also notes that CIPFA and CIPFA/LASAAC are not proposing substantial change to SeRCOP provisions.

6.2 The Secretariat's discussions with government departments have made sure that the government departments are aware of the change. A number of the discussions have highlighted the need to maintain the accuracy of the financial information reported under the relevant statistical returns which are used by the various parts of government for analysis and further reporting and statistical purposes.

6.3 The Secretariat would note that other parties also use the government statistical returns for benchmarking purposes and therefore the ITC raises this issue and the Secretariat will consider various opportunities to bringing the change to the attention of these groups.

CIPFA/LASAAC is invited to note the comments about the meetings with government departments about statistical returns

CIPFA/LASAAC is invited to consider whether it wishes to approve the comments in the ITC on the relationship of SeRCOP with government and other statistical returns.

7 Disclosures

7.1 The Streamlining review project plan includes a review of disclosures. The Secretariat considered that it might be useful to utilise the disclosure framework in FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* to identify possible areas of consideration for disclosures that may overburden local authority financial statements with too much detail. The areas identified in the previous consultations as meeting this description have been disclosures on:

7.2 **Leases** – the Secretariat did not identify any substantial areas of difference between the Code and FRS 102. The Secretariat therefore recommends no change.

7.3 **Post-Employment Benefits** - There are a number of differences between the Code under IAS 19 and FRS 102 (the disclosures under FRS 102 are very similar to the disclosures under the pre 2011 edition of IAS 19). However, FRS 102 does seem to emanate from a different risk base to that traditionally used for the measurement of local authority assets and liabilities. For example, it permits that liabilities are not measured by an actuary. As CIPFA/LASAAC decided in the 2013/14 Code to move from the pre 2011 based disclosures as it agreed with the IASB's views on the provisions (and did seek local authorities views on whether a number of the individual disclosure should or should not be included), it is recommended that the disclosures in IAS 19 should remain. CIPFA/LASAAC might wish the Secretariat to identify some of the more technical disclosures which authorities might consider to be included in a Technical Appendix.

7.4 **Heritage Assets** – the disclosures in the Code are based on FRS 102 and are in fact less onerous as CIPFA/LASAAC decided last year to reduce the five year analysis of Heritage Assets transactions to only the current and preceding year.

7.5 **Financial Instruments** - There are a number of disclosures that are not included in the Basic Financial Instrument Section of FRS 102:

- *The fair value of instruments not carried at fair value* – it is suggested that this is still an important disclosure for local authorities because of the greater incidence of borrowing and lending at fixed interest rates – therefore the difference between the carrying amount and the fair value is often substantial in local government.

- *Qualitative and Quantitative Disclosures about risk – FRS 102* only requires disclosure of risks arising from financial instruments for those held at fair value through profit or loss that are not a part of a trading portfolio and are not derivatives. Especially following the issues arising from Icelandic investments a few years ago it is arguable that the users local authorities will have a wider interests in the risks to effective stewardship of all an authority's financial instruments

- *Reclassification of financial instruments* – it is suggested that this disclosure will not be frequently used by local authorities.

- *Offsetting* – the Code Guidance Notes already indicate that these transactions are do not regularly occur for local authorities.

- *Use of Allowance accounts.*

Other than the fair value and risk disclosures discussed above there are not significant differences between FRS 102 and the Code. However, FRS 102 could be used as a model for streamlining the Code requirements, particularly in separating out basic and special disclosures (with basic and special being determined from a local government perspective).

CIPFA/LASAAC's views are sought on whether it would wish development of the post-employment benefit and the financial instruments disclosure requirements to be developed for the consultation as outlined above.

8 Transition under the New Proposals

8.1 CIPFA/LASAAC will be aware that fundamental changes to IFRS normally have a significant lead in time. The 2016/17 Code will also bring forward the substantial changes to the measurement of transport infrastructure assets. The amendments for the Streamlining Review have been drafted as if they apply for the 2016/17 year. However, the ITC raises the issue of transition for the new proposals. It notes that much of the information required by the proposals is already provided in the financial statements (or in working papers to support the financial statements). The ITC suggests that the implementation date for the proposals might be 2017/18 or possibly later subject to the feedback from the consultation.

8.2 The Secretariat is aware, however, that a number of stakeholders that are aware of the proposals would wish to adopt them as soon as possible and therefore the ITC suggests that the Code could permit early adoption eg in the 2016/17 or even possibly the 2015/16 Code. However, the Secretariat considers that if early adoption were to be permitted that it would need to be on a whole approach and not a piecemeal basis. The possible exception might be the MiRS note on the adjustments between the funding and the accounting basis. If the Board permits early adoption the amendments to Section 3.4 would need to be included in an Appendix to the Code.

CIPFA/LASAAC is invited to consider the approach in the ITC on the transitional approach to the changes.

Recommendation

CIPFA/LASAAC is asked to consider the ITC and Exposure Draft of the Code, its views on the individual sections above and approve the documents for consultation.